



BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

**Financial Statements for the Years Ended
December 31, 1998 and 1997, and
Independent Auditors' Reports**

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

TABLE OF CONTENTS

	Page
INDEPENDENT AUDITORS' REPORT ON FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 1998	1
FINANCIAL STATEMENTS FOR THE YEARS ENDED DECEMBER 31, 1998 AND 1997:	
Balance Sheets	2
Statements of Revenues and Expenses and Fund Balance	3
Statements of Cash Flows	4
Notes to Financial Statements	5-12
INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED UPON THE AUDIT PERFORMED IN ACCORDANCE WITH <i>GOVERNMENT AUDITING STANDARDS</i>	13

**INDEPENDENT AUDITORS' REPORT**

To the Board of Governors of the
Federal Reserve System:

We have audited the accompanying balance sheet of the Board of Governors of the Federal Reserve System (the Board) as of December 31, 1998, and the related statements of revenues and expenses and fund balance, and of cash flows for the year then ended. These financial statements are the responsibility of the Board's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the Board for the year ended December 31, 1997, were audited by other auditors whose report, dated March 16, 1998, expressed an unqualified opinion on those statements.

We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the 1998 financial statements referred to above present fairly, in all material respects, the financial position of the Board as of December 31, 1998, and the results of its operations and its cash flows for the year then ended in conformity with generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 20, 1999, on our tests of the Board's compliance with certain provisions of laws, regulations, contracts, and grants and our consideration of the Board's internal control over financial reporting.

Deloitte & Touche LLP
April 20, 1999

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

BALANCE SHEETS

<u>ASSETS</u>	As of December 31,	
	<u>1998</u>	<u>1997</u>
CURRENT ASSETS		
Cash	\$20,111,430	\$23,364,834
Accounts receivable	910,282	1,071,278
Transfers receivable-surplus Federal Reserve Bank earnings (Note 1)	0	652,913,560
Prepaid expenses and other assets	<u>1,215,277</u>	<u>992,096</u>
Total current assets	22,236,989	678,341,768
PROPERTY, BUILDINGS, AND EQUIPMENT, NET (Note 5)	<u>58,438,555</u>	<u>64,220,105</u>
Total assets	<u><u>\$80,675,544</u></u>	<u><u>\$742,561,873</u></u>
 <u>LIABILITIES AND FUND BALANCE</u>		
CURRENT LIABILITIES		
Accounts payable and accrued liabilities	\$8,231,187	\$9,797,829
Accrued payroll and related taxes	7,745,624	7,609,781
Transfers payable-surplus Federal Reserve Bank earnings (Note 1)	0	652,913,560
Accrued annual leave	7,493,533	7,477,187
Capital lease payable (current portion)	135,205	98,772
Unearned revenues and other liabilities	<u>2,034,129</u>	<u>2,016,190</u>
Total current liabilities	25,639,678	679,913,319
CAPITAL LEASE PAYABLE (non-current portion)	406,773	516,228
ACCUMULATED RETIREMENT BENEFIT OBLIGATION (Note 2)	773,177	740,497
ACCUMULATED POSTRETIREMENT BENEFIT OBLIGATION (Note 3)	20,721,869	20,193,034
ACCUMULATED POSTEMPLOYMENT BENEFIT OBLIGATION (Note 4)	<u>2,183,602</u>	<u>1,769,646</u>
Total liabilities	<u>49,725,099</u>	<u>703,132,724</u>
FUND BALANCE	<u>30,950,445</u>	<u>39,429,149</u>
Total liabilities and fund balance	<u><u>\$80,675,544</u></u>	<u><u>\$742,561,873</u></u>

See notes to financial statements

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

**STATEMENTS OF REVENUES AND EXPENSES
AND FUND BALANCE**

	For the years ended December 31,	
	1998	1997
BOARD OPERATING REVENUES		
Assessments levied on Federal Reserve Banks for Board operating expenses and capital expenditures	\$178,008,900	\$174,406,600
Other revenues (Note 6)	8,345,087	9,460,475
Total operating revenues	<u>186,353,987</u>	<u>183,867,075</u>
BOARD OPERATING EXPENSES		
Salaries	110,455,527	108,870,919
Retirement and insurance contributions	18,684,301	19,835,377
Contractual services and professional fees	17,913,599	10,735,745
Depreciation and net losses on disposals	13,013,690	9,306,428
Postage and supplies	6,843,836	4,261,161
Travel	5,170,630	4,680,031
Utilities	4,798,940	4,172,795
Software	4,344,064	4,130,603
Equipment and facilities rental	4,257,297	4,291,093
Repairs and maintenance	3,280,615	2,895,097
Printing and binding	2,138,315	2,707,738
Other expenses (Note 6)	3,931,877	3,665,738
Total operating expenses	<u>194,832,691</u>	<u>179,552,725</u>
BOARD OPERATING REVENUES OVER (UNDER) EXPENSES	<u>(8,478,704)</u>	<u>4,314,350</u>
ISSUANCE AND REDEMPTION OF FEDERAL RESERVE NOTES		
Assessments levied on Federal Reserve Banks for currency costs	408,544,472	363,738,623
Expenses for currency printing, issuance, retirement and shipping	408,544,472	363,738,623
CURRENCY ASSESSMENTS OVER (UNDER) EXPENSES	<u>0</u>	<u>0</u>
TOTAL REVENUE OVER (UNDER) EXPENSES	<u>(8,478,704)</u>	<u>4,314,350</u>
FUND BALANCE, Beginning of year	39,429,149	35,114,799
TRANSFERS TO THE U.S. TREASURY		
Transfers and accrued transfers from surplus Federal Reserve Bank earnings (Note 1)	18,438,855,572	20,765,972,296
Transfers and accrued transfers to the U.S. Treasury (Note 1)	<u>(18,438,855,572)</u>	<u>(20,765,972,296)</u>
FUND BALANCE, End of year	<u><u>\$30,950,445</u></u>	<u><u>\$39,429,149</u></u>

See notes to financial statements

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

STATEMENTS OF CASH FLOWS

	For the years ended December 31,	
	1998	1997
CASH FLOWS FROM OPERATING ACTIVITIES		
Board operating revenues over (under) expenses	(\$8,478,704)	\$4,314,350
Adjustments to reconcile operating revenue over (under) expenses to net cash provided by operating activities:		
Depreciation and net losses on disposals	13,013,690	9,306,428
(Increase) decrease in accounts receivable, prepaid expenses and other assets	(62,185)	2,745,993
(Increase) decrease in transfers receivable-surplus Federal Reserve Bank earnings	652,913,560	6,949,042
Increase (decrease) in accounts payable and accrued liabilities	(1,566,642)	(637,716)
Increase (decrease) in payroll payable and related taxes	135,843	805,103
Increase (decrease) in transfers payable-surplus Federal Reserve Bank earnings	(652,913,560)	(6,949,042)
Increase (decrease) in accrued annual leave	16,346	510,860
Increase (decrease) in capital lease payable	(73,022)	0
Increase (decrease) in unearned revenues and other liabilities	17,939	(247,148)
Increase (decrease) in accumulated retirement benefits	32,680	274,441
Increase (decrease) in accumulated postretirement benefits	528,835	2,021,312
Increase (decrease) in accumulated postemployment benefits	413,956	360,303
Net cash provided by operating activities	3,978,736	19,453,926
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from disposals of furniture and equipment	16,400	18,301
Capital expenditures	(7,248,540)	(11,819,651)
Net cash used in investing activities	(7,232,140)	(11,801,350)
NET INCREASE (DECREASE) IN CASH	(3,253,404)	7,652,576
CASH BALANCE, Beginning of year	<u>23,364,834</u>	<u>15,712,258</u>
CASH BALANCE, End of year	<u><u>\$20,111,430</u></u>	<u><u>\$23,364,834</u></u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Capital lease obligations incurred	<u><u>\$0</u></u>	<u><u>\$615,000</u></u>

See notes to financial statements

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 1998 AND 1997

(1) **SIGNIFICANT ACCOUNTING POLICIES**

Board Operating Revenues and Expenses--Assessments made on the Federal Reserve Banks for Board operating expenses and capital expenditures are calculated based on expected cash needs. These assessments, other operating revenues, and operating expenses are recorded on the accrual basis of accounting.

Issuance and Redemption of Federal Reserve Notes--The Board incurs expenses and assesses the Federal Reserve Banks for the costs of printing, issuing, shipping, and retiring Federal Reserve Notes. These assessments and expenses are separately reported in the statements of revenues and expenses because they are not Board operating transactions.

Property, Buildings and Equipment--The Board's property, buildings and equipment are stated at cost less accumulated depreciation. Depreciation is calculated on a straight-line basis over the estimated useful lives of the assets, which range from 4 to 10 years for furniture and equipment and from 10 to 50 years for building equipment and structures. Upon the sale or other disposition of a depreciable asset, the cost and related accumulated depreciation are removed from the accounts and any gain or loss is recognized.

Federal Reserve Bank Surplus Earnings--The Omnibus Budget Reconciliation Act of 1993 required that surplus Federal Reserve Bank earnings be transferred from the Banks to the Board and then to the U. S. Treasury for the period October 1, 1996 to September 30, 1998. Prior to October 1, 1996 and after September 30, 1998, the Federal Reserve Banks made their transfers directly to the Treasury. The Board accounted for these transfers when earned and due, which may result in transfers receivable and payable as of the balance sheet date.

Estimates--The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Reclassifications--Certain 1997 amounts have been reclassified to conform with the 1998 presentation.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 1998 AND 1997

(2) RETIREMENT BENEFITS

Substantially all of the Board's employees participate in the Retirement Plan for Employees of the Federal Reserve System (System Plan). The System Plan is a multiemployer plan which covers employees of the Federal Reserve Banks, the Board, and the Plan Administrative Office. Employees of the Board who entered on duty prior to 1984 are covered by a contributory defined benefits program under the System Plan. Employees of the Board who entered on duty after 1983 are covered by a non-contributory defined benefits program under the System Plan. Contributions to the System Plan are actuarially determined and funded by participating employers at amounts prescribed by the System Plan's administrator. Based on actuarial calculations, it was determined that employer funding contributions were not required for the years 1998 and 1997, and the Board was not assessed a contribution for these years. Excess Plan assets will continue to fund future years' contributions. The Board is not accountable for the assets of this plan.

A relatively small number of Board employees participate in the Civil Service Retirement System (CSRS) or the Federal Employees' Retirement System (FERS). The Board matches employee contributions to these plans. These defined benefit plans are administered by the Office of Personnel Management. The Board's contributions to these plans totaled \$233,000 and \$196,000 in 1998 and 1997, respectively. The Board has no liability for future payments to retirees under these programs, and it is not accountable for the assets of the plans.

Employees of the Board may also participate in the Federal Reserve System's Thrift Plan. Under the Thrift Plan, members may contribute up to a fixed percentage of their salary. Board contributions are based upon a fixed percentage of each member's basis contribution and were \$4,794,000 and \$4,772,000 in 1998 and 1997, respectively.

Effective January 1, 1996, Board employees covered under the System Plan are also covered under a Benefits Equalization Plan (BEP). Benefits paid under the BEP are limited to those benefits that cannot be paid from the System Plan due to limitations imposed by Sections 401(a)(17), 415(b) and 415(e) of the Internal Revenue Code of 1986. Pension costs attributed to the BEP reduce the pension costs of the System Plan. Activity for 1998 and 1997 is summarized in the following table:

	1998	1997
<u>Change in Benefit Obligation</u>		
Benefit Obligation at Beginning of Year	\$528,000	\$1,118,000
Service Cost	65,000	133,000
Interest Cost	21,000	81,000
Plan Participants' Contributions	0	0
Plan Amendments	0	(820,000)
Actuarial (Gain)/Loss	320,000	16,000
Benefits Paid	(36,000)	0
Benefit Obligation at End of Year	<u>\$898,000</u>	<u>\$528,000</u>

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 1998 AND 1997

	1998	1997
<u>Change in Plan Assets</u>		
Fair Value of Plan Assets at Beginning of Year	\$0	\$0
Actual Return on Plan Assets	0	0
Employer Contributions	36,000	0
Plan Participants' Contributions	0	0
Benefits Paid	(36,000)	0
Fair Value of Plan Assets at End of Year	<u>\$0</u>	<u>\$0</u>

<u>Reconciliation of Funded Status at End of Year</u>		
Funded Status	(\$898,000)	(\$528,000)
Unrecognized Net Actuarial (Gain)/Loss	(609,177)	(476,497)
Unrecognized Prior Service Cost	(424,000)	(996,000)
Unrecognized Net Transition Obligation	1,158,000	1,260,000
Prepaid/(Accrued) Postretirement Benefit Cost	<u>(\$773,177)</u>	<u>(\$740,497)</u>

Weighted-average assumptions as of December 31

Discount Rate	6.25%	7.00%
Rate of Compensation Increase	4.25%	5.00%

Components of Net Periodic Expense for Year

Service Cost	\$65,000	\$133,000
Interest Cost	21,000	81,000
Expected Return on Plan Assets	0	0
Amortization of Net Liability	103,000	103,000
Amortization of Prior Service Cost	(73,000)	(14,000)
Recognized Net Actuarial Gain	(48,000)	(29,000)
Special Termination Benefit	0	0
Total Net Periodic Expense	<u>\$68,000</u>	<u>\$274,000</u>

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 1998 AND 1997

(3) **POSTRETIREMENT BENEFITS**

The Board provides certain defined benefit health and life insurance for its active employees and retirees. Activity for 1998 and 1997 is summarized in the following table:

	1998	1997
<u>Change in Benefit Obligation</u>		
Benefit Obligation at Beginning of Year	\$22,973,898	\$21,329,126
Service Cost	133,733	154,474
Interest Cost	1,397,922	1,474,782
Plan Participants' Contributions	195,272	187,788
Plan Amendments	0	1,161,618
Actuarial (Gain)/Loss	(549,800)	(251,176)
Benefits Paid	(1,204,713)	(1,082,714)
Benefit Obligation at End of Year	<u>\$22,946,312</u>	<u>\$22,973,898</u>
<u>Change in Plan Assets</u>		
Fair Value of Plan Assets at Beginning of Year	\$0	\$0
Actual Return on Plan Assets	0	0
Employer Contributions	1,009,441	894,926
Plan Participants' Contributions	195,272	187,788
Benefits Paid	(1,204,713)	(1,082,714)
Fair Value of Plan Assets at End of Year	<u>\$0</u>	<u>\$0</u>
<u>Reconciliation of Funded Status at End of Year</u>		
Funded Status	(\$22,946,312)	(\$22,973,898)
Unrecognized Net Actuarial (Gain)/Loss	2,224,443	2,780,864
Unrecognized Prior Service Cost	0	0
Unrecognized Net Transition Obligation	0	0
Prepaid/(Accrued) Postretirement Benefit Cost	<u>(\$20,721,869)</u>	<u>(\$20,193,034)</u>
<u>Components of Net Periodic Expense for Year</u>		
Service Cost	\$133,733	\$154,474
Interest Cost	1,397,922	1,474,782
Amortization of Prior Service Cost	0	0
Amortization of (Gains)/Losses	6,621	1,286,982
Total Net Periodic Expense	<u>\$1,538,276</u>	<u>\$2,916,238</u>

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 1998 AND 1997

	1998	1997
<u>Effect of a One-Percentage Point Increase in Health Care</u>		
<u>Cost Trend Rate on:</u>		
Year-End Benefit Obligation	\$2,382,383	\$1,777,007
Total of Service and Interest Cost Components	97,751	172,488
 <u>Effect of a One-Percentage Point Decrease in Health Care</u>		
<u>Cost Trend Rate on:</u>		
Year-End Benefit Obligation	(\$1,885,077)	(\$2,536,859)
Total of Service and Interest Cost Components	(156,553)	(152,179)

The liability and costs for the postretirement benefit plan were determined using discount rates of 6.25 percent as of December 31, 1998 and 7.00 percent as of December 31, 1997. Unrecognized losses of \$2,224,443 and \$2,780,864 as of December 31, 1998 and 1997, respectively, result from changes in the discount rate used to measure the liabilities. Under Statement of Financial Accounting Standards No. 106, Employers' Accounting for Postretirement Benefits Other Than Pensions, the Board may have to record some of these unrecognized losses in operations in future years. The assumed health care cost trend rate for measuring the increase in costs from 1998 to 1999 was 8.50 percent. These rates were assumed to gradually decline to an ultimate rate of 4.75 percent in the year 2006 for the purpose of calculating the December 31, 1998 accumulated postretirement benefit obligation. The assumed salary trend rate for measuring the increase in postretirement benefits related to life insurance was an average of 5 percent.

The above accumulated postretirement benefit obligation is related to the Board sponsored health benefits and life insurance programs. During 1997, a special retirement program was offered to employees who were eligible to retire by May 31, 1998. This resulted in a curtailment loss of \$1,174,489 for 1997, comprised of \$1,044,096 for 62 employees covered by the Board sponsored health benefits plan, and \$130,393 for 78 employees covered by the Board sponsored life insurance plan. The Board has no liability for future payments to employees who continue coverage under the federally sponsored programs upon retiring. Contributions for active employees participating in federally sponsored programs totaled \$3,839,000 and \$3,667,000 in 1998 and 1997, respectively.

The medical component of the benefit obligation at end of year 1998 was \$18,538,000. Pursuant to the Federal Employees Health Care Act of 1998, on January 11, 1999, the Board paid the Office of Personnel Management \$16,100,000 to compensate the Employee Health Benefits Fund for the costs of providing future health care benefits. Coverage for Board employees and retirees enrolled in the Federal Reserve System Health Plan terminated involuntarily on December 31, 1998.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 1998 AND 1997

(4) POSTEMPLOYMENT BENEFIT PLAN

The Board provides certain postemployment benefits to eligible employees after employment but before retirement. Effective January 1, 1994, the Board adopted Statement of Financial Accounting Standards No. 112, Employers' Accounting for Postemployment Benefits, which requires that employers providing postemployment benefits to their employees accrue the cost of such benefits. Prior to January 1994, postemployment benefit expenses were recognized on a pay-as-you-go basis. The postemployment benefit expense was \$614,000 and \$516,000 for 1998 and 1997, respectively.

(5) PROPERTY, BUILDINGS AND EQUIPMENT

The following is a summary of the components of the Board's fixed assets, at cost, net of accumulated depreciation.

	As of December 31,	
	1998	1997
Land and improvements	\$1,301,314	\$1,301,314
Buildings	43,162,040	65,611,228
Furniture and equipment	46,133,411	63,486,071
	<u>90,596,765</u>	<u>130,398,613</u>
Less accumulated depreciation	(32,158,210)	(66,178,508)
Total property, buildings and equipment	<u>\$58,438,555</u>	<u>\$64,220,105</u>

Furniture and equipment and accumulated depreciation as of December 31, 1998 includes \$615,000 and \$102,500, respectively, for capitalized leases, which were acquired during 1997.

During 1998 the Board increased the threshold for capitalization of furniture and equipment from \$1,000 to \$5,000 per item. The Board expensed the undepreciated value of previously capitalized furniture and equipment not meeting the new capitalization threshold. The Board also simplified the method of capitalizing major building modifications, eliminating the previously used depreciation recovery method of reporting. For 1998, these changes increased depreciation expense \$4,033,000, decreased cost by \$44,112,000, and decreased accumulated depreciation by \$40,079,000.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 1998 AND 1997

(6) OTHER REVENUES AND OTHER EXPENSES

The following are summaries of the components of Other Revenues and Other Expenses.

	For the years ended December 31,	
	1998	1997
Other Revenues		
Data processing revenue	\$4,332,513	\$5,184,075
National Information Center	2,052,273	2,156,191
Subscription revenue	1,248,121	1,394,394
Reimbursable services to other agencies	147,491	399,426
Miscellaneous	564,689	326,389
Total other revenues	<u>\$8,345,087</u>	<u>\$9,460,475</u>
Other Expenses		
Tuition, registration and membership fees	\$1,428,717	\$1,118,683
Cafeteria operations, net	756,548	794,019
Subsidies and contributions	666,843	653,207
Miscellaneous	1,079,769	1,099,829
Total other expenses	<u>\$3,931,877</u>	<u>\$3,665,738</u>

(7) COMMITMENTS

The Board has entered into several operating leases to secure office, training and warehouse space for periods ranging from one to ten years. Minimum future commitments under those leases having an initial or remaining noncancelable lease term in excess of one year at December 31, 1998, are as follows:

1999	\$4,148,000
2000	4,851,000
2001	4,846,000
2002	4,820,000
after 2002	15,757,000
	<u>\$34,422,000</u>

Rental expenses under the operating leases were \$3,873,000 and \$3,960,000 in 1998 and 1997, respectively.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 1998 AND 1997

(8) FEDERAL FINANCIAL INSTITUTIONS EXAMINATION COUNCIL

The Board is one of the five member agencies of the Federal Financial Institutions Examination Council (the "Council"). During 1998 and 1997, the Board paid \$249,000 and \$228,000, respectively, in assessments for operating expenses of the Council. These amounts are included in other expenses for 1998 and 1997. During 1998 and 1997, the Board paid \$159,000 and \$158,000, respectively, for office space sub-leased from the Council.

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER
FINANCIAL REPORTING BASED UPON THE AUDIT PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

To the Board of Governors of the
Federal Reserve System:

We have audited the financial statements of the Board of Governors of the Federal Reserve System (the Board) as of and for the year ended December 31, 1998, and have issued our report thereon dated April 20, 1999. We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Governmental Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the Board's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Board's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

However, we noted other matters involving the internal control over financial reporting that we have reported to the management of the Board in a separate letter dated April 20, 1999.

This report is intended solely for the information and use of the Board and the Inspector General of the Board of Governors of the Federal Reserve System and is not intended to be and should not be used by anyone other than these specified parties.

Deloitte & Touche LLP
April 20, 1999